Teaching Kids -- in Stages -- About Money

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Summer's in full swing...and with it, numerous opportunities for teaching your kids or grandkids about money.

Many young people are pocketing pay from summer jobs and some have happily accepted money as graduation gifts. And there are seasonal temptations for spending, from games of chance at the local amusement park to the quest for souvenirs on vacation.

Unfortunately, many parents don't take advantage of plentiful opportunities to teach money lessons. A recent survey of 1,000 teens sponsored by brokerage Charles Schwab found that while parents talk to their kids about money, the chats aren't teaching the specifics. Only 24% of teens say they've learned responsible credit-card use from parents, while just 20% say their parents taught them to invest money wisely and make it grow.

But clearly, you don't want your young family members to pick up poor money practices that could dog them for the rest of their lives. Bankruptcy judge John Ninfo, founder of the Credit Abuse Resistance Education program for secondary school and college students, often tells young people about an accountant who came to his court with $80,000 in credit-card debt. She was book smart and money smart, Mr. Ninfo says, but couldn't shake bad habits she'd learned early.

Ready to talk dollars and sense? Here's a guide to lessons financial advisers and educators say you should begin teaching children by four key ages.

Age 5 (Elementary School)

The earliest years are the time for children to build good habits, like saving and living within their means, even if they don't understand why the behaviors are important. "At this age, [children] believe what their parents tell them," notes Laura Levine, executive director of the JumpStart Coalition for Personal Financial Literacy.

Parents can ask kindergartners to set aside a portion of their money in a piggy bank, without explaining the theory behind an emergency reserve. They can also set spending limits, by giving children an allowance and making them stick to it. You want to teach the principle that you can't spend $1.10 when you only have $1. Educators say that even at five, children will make different spending decisions depending on whose money they're using -- theirs or their parents'.

Limiting kids to cash on hand can be a good trick on family vacations. Don't buy those Mickey Mouse ears on a child's promise that he or she will "pay you back later." Instead, ask children to decide in advance how much of their money to bring along and make them stick to that limit. You might tell children how much you are willing to pay for their souvenirs and let them keep anything unspent.

Closer to home, explain how you save money on a day-to-day basis. Maybe you pick the small ice cream cone instead of the large, because it saves $1 and 200 calories. Or at the supermarket, point out that you buy generic cereal because it costs $2 less and you can't taste the difference anyway.

Age 12 (Middle School)

As children get older, they're ready for the basics of budgeting and investing.

Carl George, a Peoria, Ill., accountant and chair of the National CPA Financial Literacy Commission, says it's a good idea to ask preteens how they're spending money. Discuss their choices and priorities, and draw parallels to your life. Go over the family budget, and swap ideas for finding good deals or planning for large purchases.

A good way to ease teens into financial accountability is to ask young teens -- say, those 13 or 14 -- to squirrel away money for basic needs and file an expense statement if they want to be reimbursed, says Loretta Abrams, vice president of consumer affairs at HSBC North America. Discuss guidelines in advance and stick to them, so children don't learn to spend $100 on jeans when the rule is $50.

And consider helping preteens select ways to invest their savings, if you haven't done so already. Discuss whether to go with a low-risk certificate of deposit or money-market fund, which might return 5% a year, or a stock mutual fund with the potential for more dramatic ups and downs.

A good supplement to this lesson is reviewing your 401(k) or retirement account with your child. Explain how you juggle the tradeoff between risk and return, and show how your money has grown over time.

Age 16 (High School)

As teenagers start driving and take jobs, ask them to take charge of bigger decisions and create more elaborate budgets that plan for the unexpected.

If a child is driving, for example, ask him to shop around for the best deal on insurance and create a budget that accounts for things like oil changes and surprise repair bills.

And if your teen is collecting paychecks from a summer job, make it clear that you expect part of the money to go into savings. Kristine Dixon, director of consumer education at Charles Schwab, counsels the firm's young summer interns to save early and often. "Incorporate savings into your regular routine," she advises, "just like brushing your teeth."

One way to do this is to set up automated transfers from checking to savings, to remove the temptation to spend every cent.

CARE's Mr. Ninfo suggests asking teens to limit use of the debit and check cards associated with their accounts, since people typically spend less when they're paying cash. His guideline is to avoid plastic for any purchase less than $20 or for any item you eat or drink.

Age 18 (College)

The final step is to teach teens caution. At 18, teenagers can sign up for credit cards and enter into contracts with gyms, banks and cellphone companies. Explain the "buyer beware" principle, so teens view offers with a healthy amount of skepticism.

Be sure to talk to older teens about debt. You want your 18-year-old to understand what contributes to a good credit score, like a credit card with a low balance and a history of timely payments. And you want him or her to be aware of common pitfalls, like charging lots of small purchases (which can morph into giant monthly balances) or applying for credit too often, even when the bank is on campus giving away swag.

Above all, try to send your children to college with a sense of their own fallibility.

"There's so much to know that you can't possibly know it all," JumpStart's Ms. Levine counsels new high-school grads. "So before you make any decisions, ask questions."

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